ADVISOR PERSPECTIVES

New Research: The Secrets HNW Investors Keep from Advisors

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I interviewed Mike last week.

Tell us about your role at Capital Group, home of American Funds. How do you integrate your internal market research with that you obtain from outside vendors?

I'm proud of what we do in customer research at Capital Group, because we approach customer research differently. There are three things that make us different. The first is the sheer amount of custom research we do – data collection that is uniquely done on our behalf and that is available only to us and our customers. On any particular day, we have between two and four studies that are actively running in the field collecting data from investors and financial advisors. I think we do as much or more custom research as any other financial services company.

Even though we do a lot of our own custom research, we take great data from anywhere. We tap into the best research that has been done by our competitors, if they make it publicly available and we think it is robust. We also use research that has been done by academics, as well as what the government provides, with census data being one of the key things, and organizations like Pew Research that do great quality focused pieces of work.

The final thing that makes us unique is the type of research we do. We do use some methods that are more standard in the industry, such as surveys and occasionally focus groups. But what is unique is we combine that with ethnographic research where we talk with advisors in their offices and with investors in their homes.

We also use a lot of technology in our research. We harvest the social media conversations that are publicly available and bring in those conversations that are related to financial services. We use text analytics to look at what investors are discussing and we analyze them by sentiment, which are the degree of emotion that is associated with the different comments. We are gaining tremendous insights that are very organic and specific to what people are experiencing as they are going through financial decision-making.

That's what makes us unique and, frankly, that is why I love doing what I do.

What has been the focus of your recent efforts?

We have been focusing recently on four different audiences. The one that we've spent a lot of time on is looking at how the role of women within financial services is evolving. I believe that research has given us an edge in the industry with some of the insights about how women are becoming empowered within financial services.

The second audience is high-net worth investors and understanding their unique needs. We have also gone deep in understanding the generations: Millennials, Gen-ex and Boomers. Finally, we have focused across all those different audiences to look at the life events that are financially and emotionally acute. There are nine core life events that have those two components. Investors need support for those life events, so we have focused on them.

When I read your research, one of the interesting things you found was that high-net worth investors are often keeping secrets from their advisors. What are those secrets and how can an advisor uncover them?

There are three secrets we found in our research. To be clear, these aren't things that investors would describe as secrets. What came out in the research and in the way that we did it is that investors are not telling their advisors about these things. We started to realize that these secrets existed. We began to look for them within our research and saw the pattern.

The first was the "hidden test." That is a measure of success that an investor is using that they are not sharing with their advisor. It's something that is usually very important to them and may determine whether they stay with that advisor. The problem with it is the advisor doesn't know that they are being held up against that secret test.

The second is staying in the game. This is very common among people who have moved into retirement, and particularly those who have had very successful careers, typically high-net worth investors. They are searching for something that can keep them engaged and mentally sharp, and they are finding that outlet in the act of investing. Because it's a way of keeping them mentally sharp and relevant, they want to do it independently and not with their advisors. Those who are very engaged and staying in the game will hold a portion of their finances back from their advisor. They will use it to make a set of investments. They will be testing themselves in terms of their competence and how they are advancing in their understanding of investment. The problem is, over time, even though it started as them almost competing with themselves, it can become a competition with their advisors. That puts the relationship at risk.

The final secret, and the one that is most commonly known, it is what we call "playing the field." A lot of high-net worth advisors will have investors who will have a portion of their assets with multiple advisors, even though they are holding a primary relationship with the advisor who they interact with most often.

Historically, high-net worth investors have been Caucasian 60-year old males, members of the Baby Boomer generation. How is that profile changing?

That profile will change in the future, but it is changing slowly. It's still the profile in the market, and it will probably be so for a number of years to come. But it is inevitable that it is going to shift, because the underlying demographics are shifting. Among Americans, 77% over the age of 65 will self-identify as being white – almost 8 out of 10 people.

Look at the Millennial generation as an example – 68% of Millennials in California identify as nonwhite. In Texas it 62%. It is almost the mirror opposite as you go to the younger generation. It is inevitable; wealth is being created in those generations. Those demographic changes are going to start to show up in the high-net worth investor population.

Owning your own business has been the path to wealth and being a high-net worth investor. Among high-net worth investors, 40% own their own business. Now we are seeing that the startup of small businesses is becoming more ethnically diverse in terms of their ownership, and more of those businesses are being started up by women.

What are one or two things advisors can do to connect and build trust with the next generation of wealthy individuals, who will be more female and ethnically diverse than their predecessors?

The core job for advisors remains the same. It's having great listening skills and delivering personalized advice. The way that advisors can do this with an audience that is female and ethnically diverse is to mirror diversity in your practice. It helps to have a profile within your practice of advisors and support staff that shows the same diversity of the audience you are trying to reach.

The second thing is training to create self-awareness. Gender-smart training is very important for all advisors if they haven't gone through it already.

Lastly is the idea of getting out there and learning about what your local community is like, how it might be shifting and where some pockets of opportunity exist.

To use a personal example, I was very curious about how the demographics and economics of the city where I live are changing. I reached out to the local economic development board and the local small business association and asked them for some data. I followed up with a deeper conversation. It opened up my eyes to what types of small businesses are being started and how the demographic composition of the city I live is changing. If I were an advisor I would be following up immediately to ask how to reach out to those pockets of opportunity, and have the right types of skills within my practice to tap into those areas of growth.

What other characteristics of Baby Boomers do advisors need to consider as they grow their practices?

Boomers are starting to settle into retirement. Even though not all are financially sound, in our research we saw that 90% of Boomers said that retirement is the same as or better than they expected. There is general contentment that Boomers are experiencing as they move into retirement.

Boomers have experienced market volatility in the past, so advisors can draw on their experiences in addressing the volatility that they are certain to experience over the next period of time. Advisors should prepare to help Boomers with surprises. There's two that I'd suggest advisors focus on. The first is retirement timing. Less than half of Boomers retire when they plan. About a quarter of them retire later and about a third of them retire earlier. Life brings surprises. Sometimes you are more financially ready than you thought, and so you step into retirement early. Sometimes there are demands on your personal time and you realize that it's time to step into retirement just to meet those demands. Sometimes you are not financially ready, or you are getting reward from your work that keeps you in the workforce. But preparing Boomers for those timing surprises and helping them through those choices is the first place to start.

The other surprise is healthcare cost. Approximately 43% of Boomers say that the cost of health care in retirement is higher than they expected. When you look at the worries that Boomers have as they transition into retirement, health care is right at the top of the list.

Are members of Generation X a hidden opportunity for advisors? These individuals have already lived through at least two major market declines. What else should advisors consider when they work with Gen-X prospects?

Gen-X definitely represents a hidden opportunity. There has been a tendency to focus on only the two population bubbles – Millennials and Boomers – and ignore Gen-X. But Gen-Xers have almost seven times more investable assets then Millennials, and they are less likely to be working with an advisor than any other generation. We have this population that is in their peak-earning years, yet they are not getting the advice that they need in order to enter into retirement ready to be financially sound.

As advisors try to reach out and recognize this opportunity, they need to realize Gen-Xers are skeptical about the value of experts overall. Financial advisors receive some of that skepticism. The challenge is to build trust with Gen-X investors. You need to focus on is who they are and where they stand with their priorities.

The Gen-X generation has a "family first" attitude. As advisors reach out and try to bring Gen-X clients into their practice, you should focus on family and be hyper-present during the life changes that they will be going through that have a direct impact on their families' circumstances.

You need to include Gen-Xers in decision making. They are a generation that is defined by a do-it-yourself attitude, and that applies to virtually all areas of their life. They do more research on investments independently than any other generation. About half of them say they do a lot of research independently, even if they are working with an advisor. You need to work with that do-it-yourself attitude and treat them like a partner.

How about Millennials? How should advisors adapt their practices to work with them?

Make yourself relevant. You need to focus on the life events they are experiencing, because those life events are very tangible, personable and very real. Those life events have strong financial implications.

Millennials are between the ages of 23 and 37. They are going through a series of life events that are stacked one on top of the other that have long-term financial consequences. Those include switching jobs, buying or selling a house, getting married and having a child. During those life events money moves. Millennials are 13 times more likely to move money between advisors during a life event, and they experience a lot of them. They experience one-and-a-half life events a year where money has a potential to go into motion. That's when financial advice becomes relevant. That's the opportunity for advisors to reach out and to make sure that they are providing great support during for Millennial clients.

What were the most surprising findings from your research on how Millennials, Gen-X and Boomers approach investing?

I'll start with Millennials. The thing that surprised me the most was how traditional their values were. A lot of times Millennials get profiled as a generation that has a set of values that is very distinct and different from the traditional values that are held by their Boomer parents. But Millennials have the traditional values and aspirations as the generation before them has held. The majority of Millennials want to own a home, become a parent and get married. In fact, Millennials are a generation that places more importance on being a parent than the Gen-X generation.

There are two things that I'll say for Gen-X. They self-identity with a strong work ethic. We asked each generation what was most unique about their generation. For the Gen-X generation, it was the fact that they had a strong work ethic. That is something that sounds very noble. It also then plays into the idea that they consider themselves a do-it-yourself generation. They are able to solve things on their own, and that plays out in their attitude of not trusting experts, but certainly solving any of the issues that come in front of them by themselves.

The second surprise about Gen-Xers was that they don't think their generation is unique. I knew that going into the research, but it was surprising just how deeply held that belief is. Only 30% of Gen-Xers said they thought that their generation was unique. If you compare that to Millennials, it is almost the mirror opposite. About 70% of Millennials say their generation is unique. Gen-Xers have an insecurity about themselves as a generation.

The thing that surprised me about Boomers – and I found it to be a really positive – is just how content they are in retirement. As I said previously, 90% of Boomers say retirement is as good as or better than they expected. That's a really encouraging finding and it's great to hear that Boomers are having such a nice transition into retirement living.

Why do you think a client's generation has so much influence on their perceptions of money?

Studying generations is really interesting because it illustrates the interaction between the investor's life stage and their unique formative experiences. Financially, each generation had a very different experience as they entered the work force.

Boomers experienced job opportunities, market growth and had great opportunity for wealth creation. The Gen-X generation experienced long periods where the market was basically flat or volatile. They also faced a more crowded workforce, and most studies have shown less opportunity to move up within the work environment than Boomers faced. Millennials were scarred by the great recession. They had a hard road finding good jobs. Even though they are experiencing really strong market performance in this bull market, they are still very, very conservative, because they are coming from a context where they saw the influence of the great recession. They know how hard they had to work to get themselves into a good job where they could start to make investments.

So the generational experiences are very, very different. Going back to the Boomers, because they experienced ups and downs that basically worked on their behalf over the long term, they are much more patient and optimistic about the market. Gen-Xers are much more distrusting. They are trying to make up for lost time, because they didn't make as much money through their investments as they wish that they had. They are starting to get quite aggressive in the way that they are placing their investments and managing their overall portfolios. Millennials were scarred by the great recession, had to work hard to get ahead and are very savvy in terms of the way they manage their money. But they are also very conservative in the investments they make.

What is something an advisor can do right away to better connect with the different generational cohorts of investors?

It is really all about stepping inside their experiences and trying to relate to the investors more deeply. As advisors identify the defining experiences that investors had during their formative years, they will become predictors of the way their clients will react to the different challenges that they experience financially as they go through the different stages of life. Each generation is in a different life stage. Understanding the joys and challenges of those different life stages and talking to the investors about how they want to navigate them together with their advisor is going to be the secret of success.

There isn't one blanket statement applies to any generation. There are traits that are very unique and defining about those generations. By stepping into the experiences of each of those generations by engaging with your clients who represent those generations, you will be able to relate to them more deeply, and then you will be able to help them navigate the joys and challenges of their current life stage.

What can advisors do to prepare clients for an environment of heightened market volatility, recessionary fears and trade tensions?

In addition to what I said in response to your previous question, I would encourage advisors to be hyper- conscious of building trust now. Reach out to your clients to give them assurances and guidance, and do that in advance. If you haven't already, understood your clients' different attitudes and needs, and prepare them for the fact that they are going to be experiencing volatility and how you are going to work to meet their overall investor goals.

These generational cohorts are large and diverse. What are the limits to your research?

There is a danger in trying to generalize across millions of people. For example, Gen-Xers are 66 million people and there are 73 million Boomers. When you try to generalize to a large generation like that, you are going to be wrong very, very often.

We think of studying generations is interesting and helpful when you focus on the fact that insight comes from the interaction based on their life stages, because every generation ages and they are going to go through different life moments – what those generations experienced as they're grew into adulthood and first entered the workforce. By understanding them as a generation you can understand some of their likely tendencies as they hit the different life moments that were particularly acute for them both financially and emotionally.

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